

Internal Revenue Service  
**memorandum**

CC:TL:Br3  
DAMustone

date: OCT 13 1988

to: Harry Kadoshima, Group Manager (EPNG-5)  
Attn: Wayne Lunsford

from: Assistant Chief Counsel (Tax Litigation) CC:TL

subject: [REDACTED] - Excise taxes under I.R.C. § 4975

Wayne Lunsford of your office has requested that we provide you with our views as to whether a [REDACTED] sale and leaseback between [REDACTED] and the [REDACTED] for certain qualified plans [REDACTED] sponsors should be set up as prohibited transactions under I.R.C. § 4975. The matter has been discussed at length with Mr. Lunsford and representatives of the Department of Labor.

ISSUE PRESENTED

Whether the subject sale/leaseback is exempt from excise taxes under § 4975 because the land involved constitutes qualifying employer real property.

FACTS

This matter involves the sale and leaseback (for [REDACTED] years) of [REDACTED] of timberland between [REDACTED] and the [REDACTED]. Under this arrangement, the timber and mineral rights were reserved by [REDACTED] for the duration of the leaseback. Involved are [REDACTED] separate tracts which are located within a [REDACTED] mile radius (roughly a [REDACTED] square mile area) [REDACTED]. Overall, the transaction has proven to be quite beneficial to the trust financially.

The Department of Labor, through its Office of Enforcement, undertook an investigation of the subject transaction. In the course of this investigation, the matter was referred to the Internal Revenue Service in accordance with the Joint DOL/IRS Compliance Agreement. The IRS, however, did not conduct a separate examination. Instead, consents extending the applicable statute of limitations were obtained and the matter has since been held in abeyance pending final action by DOL.

[REDACTED] was issued a prospective exemption for the sale/leaseback by DOL effective [REDACTED]. In issuing this exemption, however, DOL did not (as is typically done in prospective exemptions involving completed transactions) require that any excise taxes

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arising under § 4975 be paid. See id. At the same time, the Pension Benefit Security Division (the Division in the Solicitor's Office generally responsible for DOL litigation under Title I of ERISA) was extremely reluctant to litigate this case. Indeed, it had indicated to the Office of Enforcement prior to the issuance of the prospective exemption that it was unwilling to litigate the case in the event that it was not resolved administratively.

#### DISCUSSION

The sole question here is whether the subject tracts constitute qualifying employer real property within the meaning of § 407(d)(4) of Title I of ERISA. If they do, the sale/leaseback is exempt from the prohibited transaction provisions of Title I by virtue of § 408(e) and hence, exempt under Title II as well by virtue of § 4975(e)(13). With respect to whether the tracts are qualifying employer real property, the central issue is whether the geographic dispersion requirement has been satisfied. See § 407(d)(4)(A). And, in making this determination here, consideration must be given not only to the surrounding economic circumstances, but to the potential effect of adverse environmental and weather conditions. Thus, resolution of this question will, by necessity, require the use of expert witnesses. According to DOL, the available experts (including Forestry Service employees) are not at all in agreement as to the economic aspects of the transaction and the potential effects of blight and other adverse conditions which can affect forestry lands generally. In short, their opinions apparently do not strongly favor the position which we would want to advocate in litigation.

Accordingly, absent expert opinion or other information from DOL which demonstrates that the case (which was originally referred to the Service by Labor) is a strong one, we do not believe that excise taxes under § 4975 should be imposed. This is especially true where, as here, the matter is quite complicated and would involve a substantial expenditure of time and resources. Our decision here is also influenced by the fact that after an extensive investigation, DOL itself was unwilling to litigate this matter. Accordingly, we recommend that the subject transaction be surveyed and closed without the imposition of excise taxes.

Sincerely,

MARLENE GROSS

By: 

DANIEL J. WILES  
Chief, Branch No. 3  
Tax Litigation Division